PENSION MANAGEMENT OVERSIGHT COMMISSION

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MEETING MINUTES[1]

Meeting Date:	**September 22, 2004**
Meeting Time:	**10:00 A.M.**
Meeting Place:	**State House, 200 W. Washington St., Room 404**
Meeting City:	**Indianapolis, Indiana**
Meeting Number:	**2**

Members Present: **Rep. Thomas Kromkowski, Chairperson; Rep. Ron Liggett; Rep. Lawrence Buell; Rep. Richard Mangus; Sen. Joseph Harrison; Sen. R. Michael Young; Sen. Allie Craycraft; Bruce Schweizer; William Gettings. Jr.; Steve Meno; Kip White.**

Members Absent: **Sen. Larry Lutz.**

Representative Thomas Kromkowski, chair of the Pension Management Oversight Commission (the Commission), called the meeting to order at 10:05 a.m. The minutes of the August 31, 2004, meeting of the Commission were approved unanimously.

I. Proposed Amendment to the Indiana Deferred Compensation Plan Statute

The Auditor of State Connie Nass presented a proposed statutory change to the Indiana Deferred Compensation Plan. Ms. Nass stated that, during her term as Auditor of State, she has worked to develop benefits for public employees, including the state's Hoosier

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[1] Exhibits and other materials referenced in these minutes can be inspected and copied in the Legislative Information Center in Room 230 of the State House in Indianapolis, Indiana. Requests for copies may be mailed to the Legislative Information Center, Legislative Services Agency, 200 West Washington Street, Indianapolis, IN 46204-2789. A fee of $0.15 per page and mailing costs will be charged for copies. These minutes are also available on the Internet at the General Assembly homepage. The URL address of the General Assembly homepage is http://www.ai.org/legislative/. No fee is charged for viewing, downloading, or printing minutes from the Internet.

S.T.A.R.T. 457 Deferred Compensation Plan. IC 5-10-1.1-7 currently authorizes political subdivisions to adopt the state's 457 plan or to set up their own 457 plans using one or more private vendors; however, they may not do both. High surrender charges assessed by most 457 plans deter political subdivisions from switching plans, even if they would like to do so. She does not know why the current exclusivity language was adopted.

Ms. Nass proposed a statutory change that would allow political subdivisions to: (1) adopt the state's 457 plan; (2) set up a 457 plan using one or more private vendors; or (3) do both. (Exhibit 1) This change is beneficial because it would allow competition at the local level and increase choices for public employees. It would allow local units to continue to offer the state's 457 plan and also adopt a private 457 plan.

Matt Brase of the Indiana Association of Cities and Towns (IACT) stated that IACT supports the statutory change.

Representative Kromkowski asked staff to prepare a bill draft incorporating the Auditor of State's proposal for the Commission's next meeting.

II. Discussion of Preliminary Draft 3332 concerning Public Safety Disability Benefits

Staff explained that Preliminary Draft 3332 (Exhibit 2) creates a presumption that a police officer, a firefighter, or an emergency medical services provider, who incurs a disability from certain cancers, or a heart or lung disease while actively employed, has incurred a disability in the line of duty. The draft allows a meeting or hearing held to rebut the presumption to be held as an executive session. The draft further provides that a line of duty disability benefit retains the status of a disability benefit for the life of the disabled member.

The Commission by unanimous consent amended Preliminary Draft 3332 to remove the words "or death" from lines 39 and 44 on page two to limit the use of the presumption to the determination of a disability.

In response to questions from Senator Young, Mary Beth Braitman of Ice Miller explained that the Internal Revenue Service (IRS) does not require the periodic reevaluation of a pensioner's line of duty disability after a pension fund's normal retirement age, so the state's public safety pension funds do not review a fund member's disability status after that date.

Preliminary Draft 3332 limits the use of the presumption to full time police officers, firefighters, and emergency medical services providers (line nine, page one), because the four statewide public safety pension funds limit their membership to full-time personnel.

The requirement at line 19, page one of Preliminary Draft 3332 that an individual not be "employed elsewhere in a similar capacity" may disqualify a person who is employed by two political subdivisions from using the presumption, although the intent in adding that language was to eliminate the presumption's use for outside private employment. Representative Kromkowski suggested that interested parties propose an amendment to Preliminary Draft 3332 to address this issue before the end of the Commission's meeting.

In response to a question from Senator Craycraft, Ms. Braitman said that part time public safety officers are not permitted to pay into any of the statewide public safety pension funds to become members.

Ms. Braitman confirmed Representative Buell's assessment that Preliminary Draft 3332 carries forward the concept established several years ago that applies a presumption of disability to certain communicable diseases contracted in the line of duty.

In response to a question by Representative Liggett, Ms. Braitman explained that, although a presumption of disability would not apply to part-time public safety employees, those employees could still establish a line of duty disability from cancer, heart disease, or a lung condition by presenting appropriate evidence.

Commission Member White asked why there would be no fiscal impact from the adoption of Preliminary Draft 3332. Ms. Braitman responded that there is no fiscal impact because the amount of the benefit is exactly the same, and the change is purely for tax purposes.

Staff asked whether Ms. Braitman had a copy of the IRS letter stating that the adoption of Preliminary Draft 3332 will allow the disability benefits to be exempt from tax. Ms. Braitman replied that a letter had not yet been drafted, but that it should be worded similarly to the letter prepared for the presumption involving communicable diseases.

Staff further asked whether an IRS determination that the disability benefits are not taxable would affect state tax collections. Ms. Braitman stated that, although an IRS determination letter would apply only to federal income tax, there would be an effect on state income tax collection because the state would follow the IRS determination.

Leo Blackwell representing the Fraternal Order of Police #86, Tom Miller representing the Professional Firefighters Union, and Matt Brase of IACT all voiced support for the bill draft.

III. Discussion of Preliminary Draft 3274 concerning Judges' 1985 Benefit System Issues

Staff explained that Preliminary Draft 3274 (Exhibit 3) allows a person serving as a full-time magistrate on July 1, 2005, and requires a person who begins serving as a full-time magistrate after that date, to become a participant in the Judges' 1985 Benefit System. The draft would allow a magistrate who is a participant in the Judges' 1985 Benefit System to purchase, at full actuarial cost, service credit for prior service covered by an Indiana public employees' retirement fund. Finally, the draft would increase the monthly benefit payable to participants, survivors, and beneficiaries of the Judges' 1985 Benefit System by the same percentages and under the same conditions as the monthly benefit is increased for members of the Public Employees' Retirement Fund (PERF).

Representative Liggett asked whether other public pension funds have automatic cost of living adjustments (COLAs). Doug Todd, the actuary for the Judges' Retirement System, described the COLAs provided by other Indiana public pension funds. COLAs for PERF, the Indiana State Teachers' Retirement Fund (TRF), and the Prosecuting Attorneys Retirement Fund are granted on an ad hoc basis by the General Assembly. The monthly benefits paid by State Excise Police and Conservation Enforcement Officers' Retirement Fund and the Legislators' Defined Benefit Plan increase by the same percentage and under the same conditions as monthly benefits are increased for members of PERF. The benefits paid by the Judges' 1977 Benefit System, the 1925 Police Pension Fund, the 1937 Firefighters' Pension Fund, and the 1953 Police Pension Fund are adjusted as the salaries on which the benefits are based are increased. The State Police Pre-1987 Plan provides that, when a retiree reaches age 55, the retiree receives a pension increase equal to one-half of the difference between the retiree's pension and the maximum monthly pension of a person retiring in that year with 20 years' service. The State Police 1987 Plan does not provide for pension adjustments after retirement. The 1977 Police

Officers' and Firefighters' Pension and Disability Fund provides for an annual increase in a member's benefit equal to the percentage increase in the Consumer Price Index with a maximum increase of three percent.

Commission Member Gettings explained that he is not in favor of a COLA for the Judges' 1985 Benefit System because of the fiscal impact of a COLA on the System's unfunded liability, judges' access to private pensions based on compensation as private practitioners before or after serving as judges, the excellent compensation judges receive while on the bench, judges' full participation in Social Security, and the amount of judges' pension benefits without a COLA.

IV. Discussion of Preliminary Draft 3276 concerning Prosecuting Attorneys' Pensions

Staff explained that Preliminary Draft 3276 (Exhibit 4) would reduce from ten to eight the number of years required to vest as a member of the Prosecuting Attorneys' Retirement Fund.

In response to a question by Commission Member White about the fiscal impact of this proposal, staff responded that Mr. Todd estimated that the unfunded accrued liability will increase by $200,000.

Senator Young asked whether this change would apply to prosecutors who have already completed their service. Mr. Todd explained that, although the draft does not have an applicability section, historically a change like this one would apply to individuals who complete their service after the effective date of the change.

Steve Johnson of the Prosecuting Attorneys' Council testified in support of the bill draft. He pointed out that judges and county constitutional officers vest in eight rather than ten years.

Representative Kromkowski directed staff to revise the bill draft for the Commission's next meeting to include an applicability provision.

V. PERF and TRF Administrative Issues

Ms. Braitman reported that PERF and TRF will not be presenting a bill draft concerning administrative issues this year.

VI. Report on the Funding Status of TRF

Dr. William E. Christopher, Executive Director of TRF, presented the TRF funding status report prepared by Gabriel Roder Smith Co. (Exhibit 5). Dr. Christopher noted that Gabriel Roder has served as TRF's actuary since 1977. He introduced Ms. Judith A. Kermans of Gabriel Roder, Mr. Matthew B. Murphy III, Director of Finance Administration for the Mays Chemical Co. and President of the TRF Board of Trustees, and Mr. Robert D. Newland, TRF's Deputy Director and Chief Investment Officer.

Dr. Christopher reviewed TRF's Mission Statement and Core Values. He discussed the differences between a prefunded plan and a pay-as-you-go plan in financing increasing benefit obligations. He reviewed a graph showing the cash benefits paid over time for the Closed TRF Pension Plan.

Dr. Christopher then summarized the benefit provisions for TRF (pp. D-1 and D-2) and the population projections for active members and retired members for the Closed and New Plans (p. H-5). He noted that the number of active members in the Closed Plan is slowly declining.

Next, Dr. Christopher highlighted the active member data for both plans (p. B-9), including the number of active members, the valuation payroll, and the average age, years of service, salary, and annual increase on the June 30 valuation date for the years 1975 through 2003. He briefly discussed the TRF comparative statistical ratios of: (1) active members per retired life; and (2) annual retirement allowances as a percent of the valuation payroll (p. B-10); and provided a historical comparison of the computed employer contribution rates (expressed as a percent of payroll) for both the Closed and New Plans (p. B-1).

Dr. Christopher reviewed historical comparisons of the percent of the actuarial accrued liability funded for the Closed Plan and the New Plan (pp. B-3 and B-4). The Closed Plan had 59% of its accrued liabilities covered by fund assets as of June 30, 2003. In dollar amounts this represents an unfunded actuarial accrued liability of $7.6 billion as of June 30, 2003 (p. B-5). The 2004 studies are not finished yet, but Dr. Christopher said that these amounts will increase.

Dr. Christopher characterized the unfunded actuarial accrued liability for the New Plan as "normal" and nothing to get excited about. The unfunded amount occurs because a member of the Closed Plan who takes a job with another covered employer joins the New Plan, and the member's unfunded liability is transferred from the Closed Plan to the New Plan.

Dr. Christopher reviewed the historical comparison for retired members and beneficiaries monthly allowances and related liability (pp. B-6 and B-7). He directed Commission members' attention to the last column which shows the ratio of reserves to liability. The ratio for the Closed Plan is 58.6%.

Pages C-2 and C-3 chart the projected payout between 2003 and 2052 for the Closed Plan. The graph on the back of page C-3 illustrates the chart. Dr. Christopher pointed out that the state financed payroll for retired members will exceed one billion dollars in 2017, and the peak payroll for retired members is estimated to be $1,232.1 million in 2026. The chart on page C-4 shows the projected payout between 2003 and 2052 for the New Plan.

The report next contains a letter dated June 3, 2004, from Ms. Kermans to Dr. Christopher showing short term projected state pension payouts for budget estimates for fiscal years 2005 through 2009 for the Closed Plan. Dr. Christopher sent copies of this letter to the Budget Agency and others. He has this information prepared each year to get a rolling look at the estimated payout amounts.

The next set of charts shows monthly benefit amounts paid by type of benefit for both the Closed and New Plans (pp. E-1 through E-4). The chart on page E-5 illustrates the erosion in the purchasing power of the monthly benefits over time. For example, the value of $100 paid to a member who retired during the year ending June 30, 1955, is now $58.12 after taking into account accumulated benefit increases, and $14.71, if the accumulated benefit increases are not included.

Dr. Christopher discussed the number of retired members tabulated by the year of retirement (pp. E- through E-6). He noted that TRF is paying benefits to five members over the age of 105.

Differences in the amount of the monthly allowance and attained age between men and women in both plans were summarized on pages E-7 and E-8. Page E-11 provides information about active members of the Closed Plan by attained age and years of service. Dr. Christopher highlighted the number of active members between ages 50 and 60 (22,058--about half of the active members in the Closed Plan), because all of these people are probably now eligible for retirement and could retire at any time.

Appendix B is an actuarial funding summary for FY 2003 for all public pension funds in the United States. It shows that TRF has the second lowest funding ratio (42.1%) of all of the funds. Only the West Virginia Teachers Fund has a lower funding ratio (19.2%).

The final chart in the report shows the history of the Pension Stabilization Fund for the years 1995-2004, including transaction descriptions, contributions, interest earned, and fund balances.

Dr. Christopher briefly discussed a supplemental handout (Exhibit 6). He noted that TRF has not had great investment earnings over the last three years (2001-2003); however, TRF's performance is in the upper decile for all public pension funds.

Dr. Christopher concluded by saying that he hoped that he had given Commission members a sense of the things that everyone should be paying attention to. His three step plan for funding TRF is: (1) Have a plan. (2) Have the discipline to stay with the plan. (3) Carefully calculate changes in the fund's commitments to its members.

In response to a question from Senator Young, Dr. Christopher stated that the total unfunded liability for both the Closed Plan and the New Plan is $8.2 billion.

Commission Member Gettings questioned how the Guaranteed Fund rate is determined. He suggested that the rate be tied to a more realistic and current rate of return, such as treasuries, or that the Guaranteed Fund money be segregated. Dr. Christopher explained that the formula used to set the Guaranteed Fund rate is based on a trailing five year average of actual earnings. The TRF Board of Trustees has looked at the Guaranteed Fund rate very closely. They have decided that the current formula provides stability to the fund members, does not cost the fund very much, and does not change the unfunded actuarial accrued liability.

Ms. Kermans added that the amount of the future obligations versus the amount of the fund reserves is very scary to an actuary.

Mr. Murphy also gave his opinion that TRF's fiscal situation is very grave.

Steve Moberly of the Indiana Retired Teachers Association commended Dr. Christopher to the Commission members. The State Board of Accounts' most recent audit did not take any exceptions to TRF's practices.

Sally Sloan of the Indiana Federation of Teachers encouraged the Commission and the legislature to stabilize TRF.

VII. Additional Discussion of Preliminary Draft 3332 concerning Public Safety Disability Benefits

Ms. Braitman presented a proposed amendment to Preliminary Draft 3332 at page one, line 19: after the word "elsewhere" insert "by the state or a political subdivision of the state". The Commission unanimously approved the amendment.

The Commission by unanimous vote recommended Preliminary Draft 3332, as amended, for introduction in the 2005 session of the General Assembly.

VIII. Next Meeting Date

Representative Kromkowski scheduled the Commission's third and final meeting for Wednesday, October 20, 2004, at 10:00 a.m. The agenda will include the adoption of a final report, a review and possible recommendation of the various bill drafts, and any other unfinished business.

Representative Kromkowski adjourned the meeting at 11:45 a.m.